IN THE

Supreme Court of the United States

OCTOBER TERM, 1976

No. 76-430

ESTATE OF HERMAN KLEIN, DECEASED, and BEBE KLEIN, MALCOLM B. KLEIN and IRA K. KLEIN, EXECUTORS, and BEBE KLEIN, Individually,

Petitioners,

—v.—

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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September 20, 1976

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

The petitioners, Estate of Herman Klein, Deceased, Bebe Klein, Malcolm B. Klein and Ira K. Klein, Executors, and Bebe Klein, individually, respectfully pray that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Second Circuit entered in this proceeding on June 29, 1976.

Opinion Below

The opinion of the Court of Appeals appears in the Appendix hereto and is not yet reported.

The opinion of the United States Tax Court is reported at 63 T.C. 585 (1975).

Jurisdiction

The judgment of the Court of Appeals for the Second Circuit was entered on June 29, 1976. This petition for a writ of certiorari was filed within 90 days of that date. This Court's jurisdiction is invoked under 28 U.S.C. §1254(1).

Questions Presented

Whether Bebe Klein is an "innocent spouse" under section 6013(e) of the Internal Revenue Code of 1954, as amended, for the tax year 1955.

Statutory Provisions Involved

"Section 6013 Joint returns of income tax by husband and wife

• • • • •

(e) Spouse relieved of liability in certain cases.

(1) In general.—Under regulations prescribed by the Secretary or his delegate, if—

(A) a joint return has been made under this section for a taxable year and on such return there was omitted from gross income an amount properly includable therein which is attributable to one spouse and which is in excess of 25 percent of the amount of gross income stated in the return.

. . . . .

then the other spouse shall be relieved of liability for tax (including interest, penalties, and other amounts) for such taxable year to the extent that such liability is attributable to such omission from gross income.

(2) Special Rules— For purposes of paragraph (1)

. . . . .

(B) the amount omitted from gross income shall be determined in the manner provided by section 6501(e)(1)(A)."

The relevant portions of sections 6013(e) and 6501(e) of the Internal Revenue Code of 1954, as amended, 26 U.S.C. §6013(e) and 26 U.S.C. §6501(e) are set forth in the Appendix.

Statement of the Case

Herman Klein and Bebe Klein, his wife, timely filed a joint return for the taxable year 1955 with the District Director of the then Upper Manhattan District, New York.

During the year 1955, Herman Klein was engaged in the manufacture of dresses as a 30% partner in the partnerships of Miss Smart Frocks and C & S Dress Company, and as a stockholder in Miss Smart Frocks, Inc.

The following items were omitted from gross income on the 1955 joint return, form 1040, filed by Herman and Bebe Klein:

Dividend Income	$21,994.29
Other Income	5,200.00
Partnership Income	18,495.74
Interest Income	43.25
Total omitted	$45,733.28

The 1955 joint return, form 1040, filed by Herman and Bebe Klein shows the following items of gross income:

Interest Income	$ 191.21
Royalty Income	494.05
Partnership Income	90,845.89
Total income reported	$91,531.15

Thus, for the taxable year 1955, the amount omitted from gross income totaling $45,733.28 exceeds 25% of the items of gross income shown on the joint return for the year 1955, form 1040, of $91,531.15.

A partnership return, form 1065, for the taxable year, beginning May 1, 1954 and ending April 29, 1955, of Miss Smart Frocks and C & S Dress Co., using the accrual method of accounting, was filed with the District Director of the then Upper Manhattan District, New York. For the year ending April 29, 1955, the partnership return of Miss Smart Frocks and C & S Dress Co. showed sales of $3,545,911.95; a schedule contained therein of C & S Dress Co. for the same year showed gross income from contracting of $141,457.40.

The joint return, form 1040, of Herman and Bebe Klein for the year 1955 did not show the items just described in the prior preceding paragraph.

The amount omitted from gross income on the joint return, form 1040, of Herman and Bebe Klein for the year 1955—$45,733.28—does not exceed 25% of the sum of $1,106,896.07, which is composed of the following items:

Interest Income	$	191.21
Royalty Income		494.05
Partnership Income (30% distributive share of gross sales and contracting income of Miss Smart Frocks and C & S Dress Co.		1,106,210.81
		$1,106,896.07

All of the above facts were stipulated to by the parties before the United States Tax Court. The full stipulation is set forth in the Appendix.

The issue of whether Bebe Klein is an innocent spouse under section 6013(e) depends upon whether the 25% test of section 6013(e)(1)(A) is 25% of the actual items of gross income reported on the 1955 joint return, $91,531.15, or 25% of the actual items of gross income reported on the 1955 joint return plus the items of gross income reported on the partnership return form 1065, $1,106,896.07. The amount omitted, $45,733.28, is greater than 25% of $91,531.15 and so Bebe Klein would be entitled to innocent spouse relief if the 25% test was 25% of the actual items of gross income reported on the joint return. But this omitted amount not being 25% of $1,106,896.07, Bebe Klein would not be entitled to innocent spouse relief if the 25% test was 25% of all items of gross income including items of gross income shown on the partnership return, form 1065.

Herman Klein died on August 30, 1964, and Bebe Klein, his wife, and Malcolm B. Klein and Ira K. Klein were appointed Executors of his estate by the Surrogate's Court of New York County on October 19, 1964.

In 1966, the within petitioners petitioned the United States Tax Court for a review of the tax deficiencies asserted against them for the years 1955-1958. The case was first referred to Commissioner Charles R. Johnston. The parties stipulated to all of the above facts and instead of holding a trial, the parties submitted their stipulation together with oral argument held on December 10, 1973 and briefs to the Commissioner.

The parties also stipulated before the United States Tax Court that Bebe Klein meets the requirements of section 6013(e)(1)(B) and (C) of the Internal Revenue Code of 1954, as amended, i.e., that she in signing the return did not know of and had no reason to know of the omissions, did not significantly benefit directly or indirectly from the items omitted from gross income, and it is inequitable to hold her liable for the deficiency.

The report of Commissioner Johnston was filed on October 15, 1974 and reported that Bebe Klein failed to meet the 25% test of section 6013(e)(1)(A) and hence was not entitled to innocent spouse relief. Judge Dawson of the United States Tax Court, in an opinion filed March 11, 1975, adopted this report with minor changes and ruled against Bebe Klein. The Decision and Order of Judge Dawson was filed on October 6, 1975.

By decision dated and Judgment entered June 29, 1976, the United States Court of Appeals for the Second Circuit upheld the decision of Judge Dawson of the United States Tax Court.

The basis for federal jurisdiction in the United States Tax Court, the court of first instance below, is section 6213 of the Internal Revenue Code of 1954, as amended, 26 U.S.C. §6213.

REASON FOR GRANTING THE WRIT

1.

The precise issue involving the meaning of the 25% test of section 6013(e)(1)(A) of the Internal Revenue Code of 1954, as amended, is an important question of federal law which has not been, but should be, settled by this Court. The meaning given to this 25% test by the Court of Appeals and United States Tax Court emasculates the innocent spouse provisions of section 6013(e) passed by Congress as ameliorative legislation, not merely for Bebe Klein but for many other otherwise innocent spouses whose spouses happen to be conducting business in partnership form.

The petitioners believe that the phrase "amount of gross income stated in the return" found in section 6013(e)(1)(A) refers only to the total of the items of gross income which were actually reported on the joint return, form 1040, and that the Court of Appeals below and the United States Tax Court committed an error of law in their holding that that phrase also included items of gross income reported on the partnership return, form 1065.

The effect of holding that the phrase "amount of gross income stated in the return" also includes amounts of gross income reported on the partnership return, form 1065, is to make it more difficult for an otherwise innocent spouse to meet the 25% test of section 6013(e)(1)(A) because the figure against which the 25% is applied is a larger figure, greater by the items of gross income shown on the partnership return, form 1065, such as gross sales, which items

are not reportable on the joint return form 1040. (On the joint return, form 1040, a taxpayer only reports his share of the net income of a partnership.)

Petitioners believe that the phrase "stated in the return" found in section 6013(e)(1)(A) only relates to the *joint return*, form 1040, and not also to the *partnership return*, for the following reasons:

A. Section 6013 is entitled "Joint returns of income tax by husband and wife."

B. Section 6013 only deals with the joint returns, form 1040, and nowhere therein is there one word about the partnership return form 1065.

C. The holding of the Court of Appeals below and the United States Tax Court has the effect of changing the phrase "stated in the return" to "stated in the returns." Yet, when Congress passed section 6013(e) the "s" was not attached to the word "return."

See *Iselin* v. *United States*, 270 U.S. 245, 250-251:

> "The statute was evidently drawn with care. Its language is plain and unambiguous. What the government asks is not a construction of a statute, but in effect an enlargement of it by the court, so that what was omitted, presumably by inadvertence, may be included within its scope. To supply omissions transcends judicial function."

See also *Gould* v. *Gould*, 245 U.S. 151, 153:

> "In the interpretation of statutes levying taxes, it is the established rule not to extend their provisions, by implication, beyond the clear import of the language used, or to enlarge their operations so as to embrace

> matters not specifically pointed out. In case of doubt they are construed most strongly against the government and in favor of the citizen."

D. The phrase "stated in the return" is preceded by the phrase "gross income" and hence qualifies the phrase "gross income" to those items of gross income reported in the return, the joint return. Section 6013(e) does not say that the amount of omitted gross income must exceed 25% of "gross income as that term is generally defined in the Internal Revenue Code of 1954, as amended."

E. Section 6013(e), the innocent spouse provision, was passed by Congress to relieve an innocent spouse of the liability for the tax deficiency, interest and penalties caused by omissions from the joint return by the other guilty spouse. Prior to its passage, the general rule was that the innocent spouse was liable for these amounts because the innocent spouse had, along with the guilty spouse, signed the return. Hence section 6013(e) is ameliorative in design and effect.

In *Helvering* v. *Bliss*, 293 U.S. 144, 150-151, this court said:

> "The exemption of income devoted to charity and the reduction of the rate of tax on capital gains were liberalizations of the law in the taxpayer's favor, were begotten from motives of public policy, and are not to be narrowly construed."

Yet the construction placed on the phrase "amount of income stated in the return" by the courts below and the Internal Revenue Service would have the effect of severely limiting the applicability of this provision to innocent

spouses of partners unlike shareholders of a close corporation because such innocent spouses must show that the amount omitted is 25% of the items of gross income reported on the joint return and the items of gross income (gross sales) reported on the partnership return, form 1065.

F. The Internal Revenue Service takes the position that the phrase "amount of gross income stated in the return" means gross income as defined in section 6501(e)(1)(A) of the Internal Revenue Code of 1954, as amended, because section 6013(e)(2)(B) states that "the amount omitted from gross income shall be determined in the manner provided by section 6501(e)(1)(A)." Section 6501 is the six year statute of limitations that gives the Internal Revenue Service the right to go back six years instead of the general rule of three years, if the taxpayer has omitted from his return an amount in excess of 25% of his gross income. Section 6501(e)(1)(A)(i) does include in gross income for purposes of the six year statute gross receipts of a partnership, *Nadine I. Davenport*, 48 T.C. 921, 928 (1967).

The petitioners contend that section 6013(e)(2)(B) does *not* require that the meaning of the phrase "amount of gross income stated in the return" be determined under section 6501(e)(1)(A) because on its face section 6013(e)(2)(B) only requires that section 6501(e)(2)(B) be consulted to determine the computation of the amount of gross income *omitted* from the return, not also the amount of gross income *stated in the return*. If section 6013(e)(2)(B) required that section 6501(e)(1)(A) be consulted to determine the "amount of gross income stated in the return," Congress could have written section 6013(e)(2)(B) as follows:

> (B) The amount omitted from gross income *and the gross income stated in the return* shall be determined in the manner provided by §6501(e)(1)(A)

But the actual wording of section 6013(e)(2)(B) is as follows:

> "(B) The amount *omitted* from gross income shall be determined in the manner provided by §6501(e)(1)(A)" (emphasis added)

Hence the construction of section 6013(e)(2)(B) by the courts below and the Internal Revenue Service is to add words to this section that are not there.

Finally, the *Davenport* rule of considering the gross sales stated on a partnership return along with the gross income on the joint return makes sense in the section 6501 area because the six year statute of limitations is an exception to the general rule of three years and the *Davenport* rule makes it more difficult for the Internal Revenue Service to go back six years. It makes no sense to incorporate this rule in the innocent spouse area where the rule would have a restrictive effect upon this ameliorative legislation.

CONCLUSION

For these reasons a writ of certiorari should issue to review the judgment and opinion of the Second Circuit.

Respectfully submitted,

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September 20, 1976

APPENDICES

APPENDICES

Opinion of the Second Circuit Court of Appeals

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

No. 823—September Term, 1975.

(Argued April 29, 1976 Decided June 29, 1976)

Docket No. 75-4257

ESTATE OF HERMAN KLEIN, Deceased, and BEBE KLEIN, MALCOLM B. KLEIN and IRA K. KLEIN, Executors, and BEBE KLEIN, Individually,

Appellants,

v.

COMMISSIONER OF INTERNAL REVENUE,

Appellee.

Before:

LUMBARD, WATERMAN and MESKILL,

Circuit Judges.

Appeal from a judgment of the United States Tax Court, Dawson, *J.*, denying appellant Bebe Klein the benefits of the "innocent spouse" provisions of Section 6013(e) of the Internal Revenue Code of 1954, 26 U.S.C. § 6013(e).

Affirmed.

PAUL M. LEVINSON, New York, New York (Henry Mayer, Mayer, Weiner & Levinson, New York, New York, of counsel), *for Appellant.*

DAVID CARMACK, Tax Division, Department of Justice, Washington, D. C. (Scott P. Crampton, Assistant Attorney General, Gilbert E. Andrews, Elmer J. Kelsey, John A. Dadeck, Jr., Tax Division, Department of Justice, Washington, D. C., of counsel), *for Appellee.*

MESKILL, *Circuit Judge:*

Bebe Klein, individually and as co-executor of the estate of Herman Klein, deceased, and Malcolm B. Klein and Ira K. Klein, the remaining co-executors of that estate, appeal from a judgment of the United States Tax Court, Dawson, *J.*, which held that Bebe Klein was not entitled to the benefits of the "innocent spouse" provisions of Section 6013(e) of the Internal Revenue Code of 1954 ("the Code"), 26 U.S.C. § 6013(e).[1] The tax court, in its opinion

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1 26 U.S.C. § 6013(e) provides as follows:

"(e) *Spouse Relieved of Liability in Certain Cases.*

(1) *In general.*—Under regulations prescribed by the Secretary or his delegate, if—

(A) A joint return has been made under this section for a taxable year and on such return there was omitted from gross income an amount properly includable therein which is attributable to one spouse and which is in excess of 25 percent of the amount of gross income stated in the return,

(B) the other spouse establishes that in signing the return he or she did not know of, and had no reason to know of, such omission, and

(C) taking into account whether or not the other spouse significantly benefited directly or indirectly from the items omitted from gross income and taking into account all other facts and circumstances, it is inequitable to hold the other spouse liable for the deficiency in tax for such taxable year attributable to such omission,

then the other spouse shall be relieved of liability for tax (including interest, penalties, and other amounts) for such taxable year to the extent that such liability is attributable to such omission from gross income.

reported at 63 T.C. 585 (1975), concluded that the "innocent spouse" protection was not available because the amount of gross income which was omitted from Herman and Bebe Klein's joint tax return for the taxable year 1955 did not exceed twenty-five percent of the amount of gross income "stated in the return" as is required by Section 6013(e)(1)(A) of the Code. We agree with the result reached by the tax court and affirm.

Section 6013(e) is designed to relieve the co-signer of a joint income tax return from liability for certain deficiencies caused by the omission from the return of a significant amount of gross income attributable to the other spouse. The applicability of this section, however, does not depend entirely on the equities of each particular situation. Rather, the "innocent spouse" must meet specific criteria in order to qualify for this statutory protection. First, the "innocent spouse" must show that in the joint return for the tax year in question "there was omitted from gross income an amount properly includable therein which is attributable to [the other] spouse and which is in excess of 25 percent of the amount of gross income stated in the return." 26 U.S.C. § 6013(e)(1)(A). It is this requirement that the tax court determined had not been met by appellant Bebe Klein. The parties stipulated that she had met the further equitable requirements, namely that "she did not know of, and had no reason to know of" the omission of income (26 U.S.C. § 6013(e)(1)(B)), and that, taking into account all of the other facts and circumstances, including whether or not she had benefited either

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(2) *Special rules.*—For purposes of paragraph (1)—

(A) the determination of the spouse to whom items of gross income (other than gross income from property) are attributable shall be made without regard to community property laws, and

(B) the amount omitted from gross income shall be determined in the manner provided by section 6501(e)(1)(A)."

directly or indirectly from the omission, it would be inequitable to hold her liable for the deficiency attributable to it (26 U.S.C. § 6013(e)(1)(C)). Consequently, the only issue presented on this appeal is whether or not the tax court correctly interpreted the requirements of subparagraph (A) as they apply to the facts in this case.

The essential facts were stipulated and so found by the tax court.[2] During the tax year involved here, 1955, Herman Klein, who died in 1964, owned a thirty percent interest in two dress manufacturing partnerships, Miss Smart Frocks and C & S Dress Company. Those partnerships filed a partnership return for the taxable year beginning May 1, 1954 and ending April 29, 1955, using the accrual method of accounting and showing gross sales receipts in the amount of $3,545,911.95 and income from contracting in the amount of $141,457.40. The partnership return further reported the partnerships' net income to be in the amount of $311,594.62, and, in Schedule K thereof, Herman Klein's distributive share of that net income to be in the amount of $90,845.89.

Herman and Bebe Klein timely filed a joint income tax return for the taxable year 1955.[3] In that return they

2 The tax court did note a contradiction between the size of the omission from income stipulated by the parties and that which it found had been omitted. It felt that the difference would have no effect upon the outcome of the case and thus gave no reasons for its finding. Since we agree that the difference will not affect the outcome, we shall give the appellants the benefit of the stipulation and use, solely for the purposes of the computations appearing later in this opinion, *supra* n. 11, the $45,733.28 figure stipulated by the parties. We express no opinion with respect to the legal accuracy of the stipulation's inclusion as an omission from gross income the $18,495.74 figure which resulted from the disallowance of certain deductions claimed by the partnerships on their return.

3 We note that the partnerships' taxable year as reported on the partnership return differs from the taxable year as reported on Herman and Bebe Klein's return, in apparent violation of the provisions of § 706(b) of the Code, 26 U.S.C. § 706(b), which require generally that a

reported interest income in the amount of $191.21, royalty income in the amount of $494.05 and partnership income in the amount of $90,845.89, which components totalled $91,531.15. The $90,845.89 figure reported as partnership income on the joint income tax return, of course, represented Herman's distributive share of the partnerships' net income as reported on the partnership return. Herman and Bebe Klein's joint income tax return omitted dividend income in the amount of $21,994.29, interest income in the amount of $43.25, "other" income in the amount of $5,200.00 and the $18,495.75 referred to in the margin,[4] for a total of $45,733.28, all of which was attributable solely to Herman Klein.

The question put squarely before us then, is whether or not the $45,733.28 concededly omitted from gross income on the joint income tax return exceeded twenty-five percent of the amount of gross income stated in the return. Appellants contend that the gross income stated in Herman and Bebe Klein's joint income tax return was $91,531.15, the actual amount reported on the Form 1040, including, insofar as the partnership income is concerned, only Herman's distributive share of the partnerships' net profits. Since the amount of gross income omitted from the return, $45,733.28, exceeds twenty-five percent of $91,531.15, they assert that the requirements of § 6013(e)-(1)(A) have been met.

The tax court and the appellee Commissioner of Internal Revenue ("Commissioner"), however, reading the joint in-

partnership and its principal partners adopt the same taxable years. Since neither the parties nor the tax court has mentioned this problem and since all arguments in this Court are based upon the assumption that Herman and Bebe Klein are liable, in their 1955 tax year, for Herman's share of the partnerships' May 1, 1954 through April 29, 1955 taxable income, we shall assume the same.

4 See *supra*, n. 2.

come tax return, Form 1040, as if it included the partnership return, Form 1065, concluded that the gross income reported by Herman and Bebe Klein was $1,106,896.07, which figure includes Herman's thirty percent distributive share, $1,106,210.81, of the partnerships' reported gross receipts income. There can be no doubt that if the tax court's approach is correct, the amount omitted from gross income does not even approach the twenty-five percent threshold required by § 6013(e)(1)(A).

It is beyond dispute that the statutory definition of gross income includes a partner's distributive share of the partnership's gross income. Sections 61(a)(13) and 702(c) of the Code, 26 U.S.C. §§ 61(a)(13) and 702(c), specifically so state.[5] These definitions, however, provide only a starting point from which to determine whether or not a partner's distributive share of the partnership's gross income is his gross income "stated" in his return for the purposes of § 6013(e)(1)(A). Appellants argue that regardless of the general statutory definition of gross income, the only gross income "stated" in the return for the purposes of § 6013(e) is that which is actually entered on the joint income tax return, Form 1040. They argue that if the legislation had been meant to include a partner's distributive share of the partnership's gross income, which is generally and properly reported only on the partner-

5 26 U.S.C. § 61(a)(13) provides as follows:

"(a) *General definition.*—Except as otherwise provided in this subtitle, gross income means all income from whatever source derived, including (but not limited to) the following items:

* * * *

"(13) Distributive share of partnership gross income."

26 U.S.C. § 702(c) provides as follows:

"(c) *Gross income of a partner.*—In any case where it is necessary to determine the gross income of a partner for the purposes of this title, such amount shall include his distributive share of the gross income of the partnership."

ship return, § 6013(e)(1)(A) would have provided that the amount omitted must be in excess of twenty-five percent of the amount of gross income "stated in the *returns*." However logical that argument may seem in the abstract, it ignores both the function of the particular return forms used in a partnership situation and the consistent line of tax court decisions which have held that, in other situations, the partnership return must be read as an adjunct to a partner's individual or joint income tax return. When one simply looks at the 1955 version of the Form 1040 and its various schedules, the reasoning behind the tax court's decisions becomes apparent.

Schedule H of Form 1040, labelled "Income from Partnerships, Estates, Trusts, and Other Sources," provides only one line for reporting partnership income together with the name and address of the partnership from which that income was derived. Schedule H speaks in terms of "[t]otal income (or loss)," the reference to losses obviously suggesting only a net (adjusted gross) rather than a gross income figure. Given that limitation upon the scope of the Form 1040, it is clear that the return neither intends nor purports to show a taxpayer's gross income when that taxpayer has partnership income. Indeed, *gross* income is not "stated in the return" in the case of such a taxpayer unless one looks at the partnership return as being a part of the personal income tax return. Appellants' argument would in essence have us read the term *gross* income out of § 6013(e)'s requirements and insert instead merely "income" or "adjusted gross income." We cannot so read the statute.

Nor does the inclusion of the partnership return as an adjunct to the joint return require a subversion of Congressional intent by changing the singular "return" in § 6013(e)(1)(A) to the plural as alleged by the appellants.

That argument misconceives both the status of partnerships within the tax structure as set forth in the Code and the function of the partnership return. A partnership, while it may be more or less a definite entity depending upon the jurisdiction in which it is located, and while it may or may not own property or commence legal actions in its own right, is simply not a taxable entity under the Code. 26 U.S.C. § 701.[6] That being the case, the return required to be filed by a partnership, 26 U.S.C. § 6031, is not an income tax return. It is essentially an information return. *See* 6 J. Mertens *Law of Federal Income Taxation* (1975 Rev.), § 35.91 at 265; *Jack Rose,* 24 T.C. 755, 768-69 (1955); *cf. Elliott J. Roschuni,* 44 T.C. 80, 84-86 (1965). There would be little reason for Congress to require a nontaxable entity, here a partnership, to file a return if that return were not to be read with the personal returns of the very taxpayers who derive their income from the partnership. The partnership return's primary function is to provide information to the Commissioner with respect to the individual returns of the partners. In effect, the partnership return must be read together with, or as an adjunct to the partner's personal income tax return in order for it to have any value at all. We fail to see why that function should be altered by our holding that the partnership return is unavailable to determine the extent of a partner's gross income "stated in [his] return."

As the tax court pointed out, § 6013(e)(2)(B)[7] itself provides convincing support for the Commissioner's posi-

6 26 U.S.C. § 701 provides as follows:

"A partnership as such shall not be subject to income tax imposed by this chapter. Persons carrying on business as partners shall be liable for income tax only in their separate or individual capacities."

7 See *supra*, n. 1.

tion. That part of the innocent spouse section directs that the determination of "the amount omitted from gross income" should be made in "the manner provided by section 6501(e)(1)(A) [26 U.S.C. § 6501(e)(1)(A)]," [8] the section which determines whether or not the Commissioner will be able to extend to six years the general three year statute of limitations. The purpose of § 6501(e)(1)(A) is to extend the statute of limitations for the assessment or collection of income taxes in situations literally identical to those required in the innocent spouse provision, namely, where the taxpayer "omits from gross income an amount properly includible therein which is in excess of 25 percent of the amount of gross income stated in the return . . . ." According to subparagraph (ii) of § 6501 (e)(1)(A), an amount is not "omitted from gross income stated in the return" if it is "disclosed in the return, or in a statement attached to the return, in a manner ade-

8 26 U.S.C. § 6501(e)(1)(A) provides as follows:

"(e) *Substantial omission of items.*—Except as otherwise provided in subsection (e)—

(1) *Income taxes.*—In the case of any tax imposed by subtitle A—

(A) *General rule.*—If the taxpayer omits from gross income an amount properly includible therein which is in excess of 25 percent of the amount of gross income stated in the return, the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time within 6 years after the return was filed. For purposes of this subparagraph—

(i) In the case of a trade or business, the term 'gross income' means the total of the amounts received or accrued from the sale of goods or services (if such amounts are required to be shown on the return) prior to diminution by the cost of such sales or services; and

(ii) In determining the amount omitted from gross income, there shall not be taken into account any amount which is omitted from gross income stated in the return if such amount is disclosed in the return, or in a statement attached to the return, in a manner adequate to apprise the Secretary or his delegate of the nature and amount of such item."

quate to apprise the Secretary or his delegate of the nature and amount of such item." Essentially, § 6501(e)(1)(A)(ii) directs that anything that is "disclosed" in the return is not "omitted" from the return. It would seem to be a truism that if an amount is "disclosed" in the return, it is somehow "stated" in the return. To that effect, it seems only logical that one must read the partnership return in order to discover whether or not an item of a partner's gross income has been "disclosed," i.e., not "omitted." If one could not look at the partnership return for that purpose, a partner's actual gross income (his distributive share of the partnership's gross income) would always be "omitted" from his return since that figure appears only on the partnership return. Such a result could not have been intended by Congress. Congress could not have intended that the statute of limitations be extended against a taxpayer when that taxpayer has properly reported all of his items of gross income. Yet that would be the technical result if the partnership return were to be isolated from examination in determining what gross income was "disclosed" in the partner's return for the purposes of § 6501(e)(1)(A)(ii).[9] We fail to see why something which must be considered to have been "disclosed" and therefore not "omitted" from the return for purposes of § 6501(e)(1)(A)(ii), should not also be considered "stated" in the return for the purposes of both

9 To be even more technical, of course, since the net income amount actually entered on the personal return is part of the partner's statutory gross income, only the difference between his share of the partnership's gross income and the net amount actually entered on the personal return would be "omitted." We would expect, however, that such difference, as in the instant case, would far exceed twenty-five percent of the net figure actually entered on the personal return in most cases. We further note that we share the tax court's opinion that the example in Treas. Reg. § 1.702-1(c) appears to conflict with § 6501(e)(1)(A)(ii)'s method for determining the amount "omitted" from gross income when a partnership return has been filed.

that section and, through § 6013(e)(2)(B)'s reference, the "innocent spouse" provision.

As mentioned at the outset, since the enactment of the 1954 Code, the tax court has consistently rejected the specific construction urged by the appellants in this case. Compare *L. Glenn Switzer*, 20 T.C. 759, 766-68 (1953) (accepting such an argument under the 1939 Code), with *Jack Rose, supra*, 24 T.C. at 768-70 (apparently, again under the 1939 Code, rejecting the argument in dictum and noting that the Court of Appeals for the Ninth Circuit has vacated *Switzer* upon the stipulation of the parties); *Elliott J. Roschuni, supra*, 44 T.C. 80 (involving the return of a duly qualified Subchapter S corporation under the 1954 Code); *Genevieve B. Walker*, 46 T.C. 630, 637-38 (1966); *Nadine I. Davenport*, 48 T.C. 921, 928 (1967). In each case after *Switzer*, the tax court has recognized that one must look to the partnership return to determine the amount of a partner's gross income not only "omitted" from his return but also "stated" in his return. We see no reason to overrule this reasoned line of cases indirectly by holding that what is "stated" in the return for "innocent spouse" purposes, is only the figure actually entered on the Form 1040.

Finally the tax court, in supporting the conclusion that the partnership return must be read together with the personal return and in computing the amount of the partnership's gross income, relied upon the definition of gross income from a trade or business as "gross receipts," which definition is contained in subparagraph (i) of § 6501(e)(1)(A).[10] The appellants have challenged the applicability of that particular subparagraph by arguing, inter alia, that since the innocent spouse section, § 6013(e)(2)(B), refers to the statute of limitations section, § 6501(e)(1)

10 See *supra*, n. 8.

(A), only for the purpose of determining what is "omitted" from gross income, the reference is limited to subparagraph (ii) of § 6501(e)(1)(A). They argue that subparagraph (i) is irrelevant in determining what is "omitted." Although appellants' argument is persuasive, we feel no need to entertain it here. Since, as we have shown above, it is not necessary to rely upon subparagraph (i) in order to conclude that the partnership return must be read as an adjunct to a partner's personal return, and since appellants have not demonstrated any independent prejudice resulting from the use of the "gross receipts" definition,[11] we shall leave the resolution of this difficult question to some future case where its resolution will affect the outcome.

Accordingly, the order of the tax court denying the benefits of "innocent spouse" status to appellant Bebe Klein is affirmed.

11 The appellants cannot be heard to complain that the tax court's use of §6501(e)(1)(A)(i)'s "gross receipts" definition of gross income in this case resulted in any prejudice to Bebe Klein's attempt to fit within the innocent spouse provisions. Section 6501(e)(1)(A)(i) defines gross income from a trade or business to include gross receipts from sales prior to diminution by the cost of the goods sold. In the instant case, even if we were to accept appellants' argument, which never alleges any particular prejudice, and subtract the cost of the goods sold as reported by Miss Smart Frocks, see Treas. Reg. § 1.61-3, its gross income on the return would have been $585,422.19, which added to C & S Dress Co.'s "contracting" income of $141,547.40, results in a total partnership gross income of $726,969.59. Herman Klein's thirty percent distributive share of that partnership gross income is then $218,090.88, and twenty-five percent of that gross income stated in the return is $54,522.72. Since the parties stipulated that only $45,733.25, which is obviously less than $54,522.72, was "omitted" from gross income stated in the return, appellants have simply not demonstrated that Bebe Klein has been harmed by the tax court's use of the "gross receipts" definition of gross income contained in § 6501(e)(1)(A)(i). She would have failed to meet the twenty-five percent requirement even if that definition had not been used.

Opinion of Judge Dawson of the United States Tax Court

63 T. C. No. 56

UNITED STATES TAX COURT

Docket Nos. 2696-64 and 2202-66.

Filed March 11, 1975.

ESTATE OF HERMAN KLEIN, Deceased, BEBE KLEIN, MALCOLM B. KLEIN and IRA K. KLEIN, Executors and BEBE KLEIN, Individually,

Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

Deceased taxpayer was a partner, with a 30 percent interest, in two partnerships. A partnership return was filed showing gross receipts from sales and contracting income in the amount of $3,545,911.45. The deceased taxpayer and his surviving spouse filed a joint Federal income tax return showing items of gross income in the total amount of $91,531.15, of which $90,845.89 was partnership gross income. The amount omitted from the joint return was $45,733.28. Petitioners contend the "amount of gross income stated in the return" was $91,531.15. Respondent contends it was $1,106,896.07. The determination of whether petitioner-wife is entitled to the benefit of

the "innocent spouse" provision of section 6013(e)(1)(A) depends upon the resolution of this issue.

Held:

1. The meaning of the phrase "amount of gross income stated in the return" used in section 6013(e)(1)(A), I.R.C. 1954, must be determined by reference to section 6501(e)(1)(A) as required by section 6013(e)(2)(B).

2. Section 6501(e)(1)(A) defines "gross income" in the case of a trade or business as the total of the amounts received or accrued from the sale of goods or services prior to diminution by the cost of such sales or services and includes in the amount of gross income stated in the return any amount which is disclosed in the return or attached to the return, in a manner adequate to apprise the secretary or his delegate of the nature and amount of such item.

3. The total of the amounts received from the sale of goods and services prior to diminution by the cost of such goods and services disclosed in the return of the partnership in the amount of $1,106,210.81 is included in the amount of gross income ($1,106,896.07) stated in the joint return of the deceased taxpayer and the surviving spouse. *Genevieve B. Walker*, 46 T.C. 630 (1966).

4. Since $45,733.28 is not in excess of 25 percent of the amount stated in the joint return, the surviving spouse does not qualify for relief under section 6013(e).

5. The gross receipts requirement does not establish an arbitrary and unreasonable classification. Thus, section 6013(e) is not unconstitutional.

Henry Mayer and *Paul M. Levinson*, for the petitioners.

Powell W. Holly, Jr. and *Kimball K. Ross*, for the respondent.

DAWSON, *Judge*: The severed issues in these cases were assigned to and heard by Commissioner Charles R. Johnston pursuant to Rules 180 and 182, Tax Court Rules of Practice and Procedure. With minor modifications the Court agrees with and adopts the report of Commissioner Johnston which is set forth below.

OPINION OF THE COMMISSIONER

Respondent determined the following deficiencies and additions to tax against petitioners for the taxable years 1955 through 1960:

Docket No.	Year	Deficiencies	Additions to Tax under sec. 6653(b)[1]
2696-64	1959	$ 9,547.71	$ 5,266.92
	1960	14,367.61	7,183.81
2202-66	1955	$48,594.11	24,762.81
	1956	14,224.40	7,598.20
	1957	11,234.48	6,142.87
	1958	7,062.26	4,056.34

[1] All statutory references are to the Internal Revenue Code of 1954, as amended, unless otherwise stated.

Upon motion by respondent, without objection by petitioners, these cases were consolidated for trial, briefs and opinion.

The principal issue to be decided herein is whether there was omitted from gross income an amount properly includable in the joint return of Herman Klein and Bebe Klein for the taxable year 1955 which is attributable to Herman Klein and which is in excess of 25 percent of the amount of gross income stated in the return as provided in section 6013(e)(1)(A). The parties have stipulated that Bebe Klein meets the requirements of section 6013(e)(1)(B) and (C) and that she is not liable for any addition to tax under section 6653(b) for the taxable year 1955.

Findings of Fact

All the facts have been stipulated and are found accordingly.

The petitioners are the Estate of Herman Klein, Deceased, Bebe Klein, Malcolm B. Klein and Ira K. Klein, Executors and Bebe Klein, as surviving wife. The addresses of the above-named individuals at the time of the filing of the petition were as follows:

Bebe Klein	201 East 83d Street New York, New York
Malcolm B. Klein	31 Dorchester Street Huntington Station, New York
Ira K. Klein	107 Jackson Place Paramus, New Jersey

Herman Klein died August 30, 1964. The Surrogates Court of New York County, New York on October 19, 1964,

granted letters testamentary on the Estate of Herman Klein to Bebe Klein, Malcolm K. Klein and Ira K. Klein who duly qualified and were acting as Executors at the time of the submission of this proceeding.

Herman Klein, during the year 1955, was engaged in the manufacture of dresses as a 30 percent partner in the partnerships of Miss Smart Frocks and C & S Dress Company, and as a stockholder in Miss Smart Frocks, Inc. A partnership return, Form 1065, for the taxable year beginning May 1, 1954, and ending April 29, 1955, of Miss Smart Frocks and C & S Dress Company, using the accrual method of accounting, was filed with the District Director of the Upper Manhattan District, New York, New York. For the year ending April 29, 1955, the partnership return of Miss Smart Frocks and C & S Dress Company showed sales in the amount of $3,545,911.95 and a schedule for the C & S Dress Company included in the partnership return showed gross income from contracting in the amount of $141,457.40. The petitioners' joint income tax return for the taxable year 1955 did not show the amount of partnership sales or the amount of gross income from contracting, included in the partnership return.

Herman Klein and Bebe Klein timely filed a joint return for the taxable year 1955 with the District Director of the Upper Manhattan District, New York. The joint return showed the following items of gross income:

Interest	$ 191.21
Royalties	494.05
Partnership	$90,845.89
Total	$91,531.15

The joint income tax return of Herman and Bebe Klein for the taxable year 1955 failed to include the following items in income, all of which are attributable to Herman Klein.

a. Dividend Income	$21,994.29
b. Other Income	5,200.00
c. Interest Income	43.25

In addition to the preceding items, the petitioners' joint income tax return failed to include in income, Herman Klein's proportionate share of corrected net partnership income from Miss Smart Frocks and C & S Dress Co. for the taxable year ended April 29, 1955, in the amount of $18,495.74 which resulted from the disallowance of various claimed deductions on the partnership return.

Ultimate Findings of Fact

The petitioners omitted the following items from gross income on their joint income tax return for the taxable year 1955:

Dividend	$21,994.29
Other income	5,200.00
Interest income	43.25
Total	$27,237.54[2]

The net partnership income of $90,845.89 from Miss Smart Frocks and C & S Dress Co. reported by Herman

[2] We note the conflict between the amount stipulated as omitted from the gross income stated in the joint return and the amount found here. However, since resolution of the conflict would not affect the result, we disregard it.

Klein on his joint income tax for the taxable year 1955 was properly increased by $18,495.74 representing his proportionate share of deductions of Miss Smart Frocks and C & S Dress Co. which were disallowed for the taxable year ended April 29, 1955.

The joint income tax return for the taxable year 1955 filed by the petitioners reported the following items of gross income:

Interest	$ 191.21
Royalties	494.05
Distributive share of gross income of partnership, Miss Smart Frocks and C & S Dress Co.	$1,106,210.81
Total gross income reported	$1,106,896.07

The amount omitted from gross income does not exceed 25 percent of the sum of $1,106,896.07.

Petitioner, Bebe Klein, does not meet the requirements of Code §6013(e)(1)(A) with respect to the taxable year 1955, nor does she qualify as an innocent spouse for the taxable year 1955 under the provisions of Code §6013(e).

Opinion

The petitioners contend that the amount omitted from gross income was "in excess of 25 percent of the amount of gross income stated in the return". They base this contention on the grounds that the amount of gross income stated in the joint return of Herman Klein and Bebe Klein was $91,531.15 and the amount omitted was $45,733.28.

Respondent stipulated that the amount omitted from the joint return was $45,733.28. However, the respondent contends that the "amount of gross income stated in the return" is $1,106,896.07. He computes this sum as follows:

Interest	$ 191.21
Royalties	494.05
Partnership (30 percent distributive share of the sales and contracting income of Miss Smart Frocks and C & S Dress Company)	$1,106,210.81
Total	$1, 106,896.07

The difference between the parties arises over the meaning of the phrase "amount of gross income stated in the return" found in section 6013(e)(1)(A).[3]

[3] SEC. 6013. JOINT RETURNS OF INCOME TAX BY HUSBAND AND WIFE. (e) Spouse Relieved of Liability in Certain Cases.—

(1) In General.—Under regulations prescribed by the Secretary or his delegate, if—

(A) a joint return has been made under this section for a taxable year and on such return there was omitted from gross income an amount properly includable therein which is attributable to one spouse and which is in excess of 25 percent of the amount of gross income stated in the return,

(B) the other spouse establishes that in signing the return he or she did not know of, and had no reason to know of, such omission, and

(C) taking into account whether or not the other spouse significantly benefited directly or indirectly from the items omitted from gross income and taking into account all other facts and circumstances, it is inequitable to hold the other spouse liable for the deficiency in tax for such taxable year attributable to such omission, then the other spouse shall be relieved of liability for tax (including interest, penalties, and other amounts) for such taxable year to the extent that such liability is attributable to such omission from gross income.

(2) Special rules.—For purposes of paragraph (1)—

(A) the determination of the spouse to whom items of gross income (other than gross income from property) are attributable shall be made without regard to community property laws, and

(B) the amount omitted from gross income shall be determined in the manner provided by section 6501(e)(1)(A).

Petitioners argue that the language of section 6013(e)(1)(A) is so clear and unambiguous that the term "amount of gross income stated in the return" can only have reference to the amount of gross income the taxpayer actually reported in the joint return. There would be much force in this point if the words could be taken out of their particular setting. However, we cannot determine the meaning of the phrase by looking at section 6013(e)(1)(A) alone because section 6013(e)(2)(B) links section 6013(e) with section 6501(e).[4] Viewed in this light, we think petitioners' argument must fall, for to accept it would render section 6013(e)(2)(B) meaningless.

Petitioners further argue that section 6013(e)(2)(B) only incorporates the adequate disclosure requirements under 6501(e)(1)(A) which determine whether an amount, and

[4] Sec. 6501. LIMITATIONS ON ASSESSMENT AND COLLECTION.

(e) Substantial Omission of Items.—Except as otherwise provided in subsection (c)—

(1) Income Taxes.—In the case of any tax imposed by subtitle A—

(A) General Rule.—If the taxpayer omits from gross income an amount properly includible therein which is in excess of 25 percent of the amount of gross income stated in the return, the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time within 6 years after the return was filed. For purposes of this subparagraph—

(i) In the case of a trade or business, the term "gross income" means the total of the amounts received or accrued from the sale of goods or services (if such amounts are required to be shown on the return) prior to diminution by the cost of such sales or services; and

(ii) In determining the amount omitted from gross income, there shall not be taken into account any amount which is omitted from gross income stated in the return if such amount is disclosed in the return, or in a statement attached to the return, in a manner adequate to apprise the Secretary or his delegate of the nature and amount of such item.

how much of an amount, has been omitted from gross income but does not incorporate the rules under section 6501 (e)(1)(A) which relates to the computation of "the amount of gross income stated in the return." They contend that section 6013(e)(2)(B) only requires the use of section 6501 (e)(1)(A) to determine how to compute the amount of omission and not how to compute "the amount of gross income stated in the return." We fail to see how a computation can be made under section 6501(e)(1)(A) of the amount of gross income omitted from a return without a simultaneous determination of the amount of gross income stated in the return; and, the only way "the amount of gross income stated in the return" can be determined, where a partner of a partnership which has filed a return is concerned, is to consider the partnership return together with the individual return in determining "the total gross income stated in the return" of the individual partner. *Genevieve B. Walker,* 46 T.C. 630 (1966). See *Nadine I. Davenport,* 48 T.C. 921, 928 (1967); *Accord, Elliott J. Roschuni,* 44 T.C. 80 (1965), and *Jack Rose,* 24 T.C. 755 (1955). Cf. Section 702(c); Section 1.702-1(c)(2), Income Tax Regs.

Petitioners also contend that the legislative history of section 6013(e) supports their position, finding particular comfort in the first sentence of the report of the Finance Committee.[5] As we read the first sentence we think "the

[5] The first requirement, that the amount omitted from gross income must equal more than 25 percent of the gross income shown on the return, is intended to limit the relief provided in the bill to those cases where the income omitted represents a significant amount relative to the reported income. Whether or not an omission meets this test is to be determined in a manner similar to the test applied under existing law in determining, for purposes of the six-year statute of limitations, when an omission in excess of 25 percent of gross income exists. S. Rept. No. 1537, 91st Cong. p. 3 (1970), 1971-1 C.B. 606, 607.

income reported" by a partner includes his share of the gross income, as defined in section 6501(e)(1)(A)(i), of the partnership. Rev. Rul. 55-415, 1955-1 C.B. 412 and I. T. 3981, 1949-2 C.B. 78.[6]

Petitioners next argue that the policy considerations behind section 6501(e) and 6013(e) are different. They point out that section 6013(e) was passed as an amelioratory provision to provide relief for an innocent spouse and that the use of the gross receipts test of section 6501 reduces the chances of an innocent spouse being able to show that the omission exceeded 25 percent of the inflated figure. However appealing this argument may be toward tempering a harsh result, we point out again that if Congress had wished to use the gross income actually reported on the joint return as the amount against which the 25 percent omission was to be measured, it need not have adopted subsection (2)(B) of 6013(e).[7] See *Ann B. Resnick,* 63 T.C. No. 48 (February 3, 1975).

[6] Respondent cites section 702(c) and section 1.702-1(c)(2), Income Tax Regs., in support of this position. We note in passing our belief that the example given in section 1.702-1(c)(2) Income Tax Regs. conflicts with section 6501(e)(1)(A)(i) and (ii) because under the latter section "gross income" is specially defined and if a partnership return is filed the entire amount of such "gross income" allocable to a partner is deemed reported on the return. We do not think the gross income referred to in section 702(c) is the equivalent of the "gross income" defined under sec. 6501(e)(1)(A).

[7] We also point out that it is not only an innocent spouse, whose guilty spouse is a member of a partnership, who is affected by a determination that other gross income is imputed to the individual return. The rule would also encompass innocent spouses of sole proprietors, *Alvin Howse,* T.C. Memo. 1974-225; and innocent spouses of shareholders of Subchapter S corporations. Cf. *Elliott J. Roschuni,* 44 T.C. 80 (1965). Respondent correctly points out that to interpret the statute in the manner contended for by petitioners, spouses of partners would be treated differently than sole proprietors and Subchapter S shareholders.

Another contention made by petitioner is that if Congress had intended that section 6501(e)(1)(A) be used to determine "the amount of gross income stated in the return" it would have worded section 6013(e)(2)(B) as follows:

> The amount omitted from gross income and the gross income stated in the return shall be determined in the manner provided by §6501(e)(1)(A).

We must disagree with petitioners since we think section 6501(e)(1)(A)(i) and (ii)[8] directly deals with the determination of the gross income stated in the return. This is because the partnership return must be read as an adjunct with the individual partner's return in determining the total gross income stated in the individual's return. Indeed, that determination with respect to partnerships arose from the gloss upon the section by the decided cases, compare *L. Glenn Switzer*, 20 T.C. 759 (1953) with *Genevieve B. Walker, supra*, and *Nadine I. Davenport, supra; Cf. Elliott J. Roschuni, supra;* and *Jack Rose, supra.*[9]

Finally, petitioners contend that the gross receipts test sets up an arbitrary, capricious, unreasonable and unfair classification because an otherwise innocent spouse would be unable to avail herself of the provisions of section 6013

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[8] Ibid., Footnote 4, (i) and (ii).

[9] See also *Harry Laudau*, 21 T.C. 414 (1953); *Norman Rodman*, T.C. Memo. 1973-277; and *Vernie S. Belcher*, T.C. Memo. 1958-180 where it is pointed out that a "partner's share of the gross income on the partnership returns must be imputed to the individual return." And that if the partnership return is not in evidence it is impossible to know the "gross income stated in the return." The six year limitation does not apply if disclosure "is made on or *with the tax return.*" (Emphasis supplied). H. Rept. No. 1337, 83d Cong. 2d Sess., p. 107 (1954); S. Rept. No. 1622, 83d Cong., 2d Sess., pp. 143-144 (1954).

(e) when the guilty spouse was a partner in a partnership that had substantial gross receipts with little or no net income or relatively little net income compared with the gross receipts of the business. They urge that the gross receipts test is wholly unrelated to the economic reality of the taxpayers' situation and therefore its use as a basis for establishing classification is arbitrary, capricious, unreasonable and unfair and hence violates due process of law under the Fifth Amendment to the United States Constitution.

In *Penn Mutual Indemnity Co.*, 32 T.C. 653, 658 (1959) this Court said:

> An act of Congress is not lightly to be set aside, and doubt must be resolved in its favor. So much is familiar learning. Moreover, the presumption in favor of validity is particularly strong in the case of a revenue measure. • • •

It is with this injunction we approach petitioners' arguments on the constitutionality of the application of section 6013(e) under the facts of this case.

We certainly must agree with the proposition stated in the cases cited by petitioners that a federal taxing statute may be so arbitrary and capricious as to cause it to fall before the due process of law clause of the Fifth Amendment. *Heiner* v. *Donnan*, 285 U.S. 312 (1932); *Brushaber* v. *Union Pacific Railroad Co.*, 240 U.S. 1 (1916); *Moritz* v. *Commissioner*, 469 F. 2d 466 (C.A. 10, 1972), reversing 55 T.C. 113; and *Reed* v. *Reed*, 404 U.S. 71 (1971). However, we point out that in both *Moritz* and *Reed, supra*, the invidious discrimination was based on sex. Under section 6013(e) both qualified male and female spouses are entitled

to the benefits of the section. For that reason we do not think either *Moritz* or *Reed* are controlling here.

Section 6013(e) is a mitigation provision and in common with other mitigation provisions not every taxpayer or transaction is entitled to relief. Cf. Section 1311 et seq. See *Knowles Electronics Inc.* v. *United States,* 365 F. 2d 43 (C.A. 7, 1966). The fact that petitioner Bebe Klein suffers a financial hardship if she is found not to be eligible for the relief provided under section 6013(e) should not be controlling.[10]

But the question here is whether in the application of section 6013(e) in conjunction with section 6501(e)(1)(A) to spouses of partners (as well as other spouses as indicated below) that section 6013(e) must fall before the Fifth Amendment as an arbitrary classification.

In *United States* v. *Maryland Savings-Share Insurance Corp.,* 400 U.S. 4, 6 (1970) the Court stated:

> • • • Normally, a legislative classification will not be set aside if any state of facts rationally justifying it is demonstrated to or perceived by the courts. [Citations omitted] • • •

We do perceive a rational basis for the classification. Congress chose as the basis for measuring the amount omitted from gross income under section 6013(e)(1)(A)

[10] • • • What warrants specialized treatment such as those which have been indicated? Mention of hardship and financial loss is unconvincing. The world at large and the income tax world in particular are full of hardship and loss despite which it is deemed sound policy to enforce general rules inflexibly. • • • Maguire, Surrey and Traynor, Section 820 of the Revenue Act of 1938. 48 Yale Law Journal 509 (1939).

the provisions of section 6501(e)(1)(A)(ii) which had been used to measure omissions from gross income in determinations of whether a three year or six year statute of limitations applied. Since Congress restricted its relief under section 6013(e) to cases involving omissions from gross income, the use of a gross receipts test in the case of a trade or business was proper.

The gross receipts test in section 6501(e)(1)(A) was adopted by Congress to eliminate some of the problems which arose under its predecessor, section 275(c) I.R.C. 1939. See *The Colony, Inc.* v. *Commissioner of Internal Revenue,* 357 U.S. 28 (1958) and the case cited therein. In *Uptegrove Lumber Co.* v. *Commissioner,* 204 F. 2d 570 (C.A. 3, 1953), the Court found there was "a real ambiguity" in section 275(c) I.R.C. 1939. The committee reports give no indication as to why a gross receipts test was adopted.[11] It can only be presumed that it was for the purpose of avoiding litigation as to whether adequate information was given as to the amount of "gross income." Cf. *L. Glenn Switzer, supra;* and *Emma B. Maloy,* 45 B.T.A. 1104 (1941). Of course, when section 6501(e)(1)(A) is applied with respect to a taxpayer who is a member of a partnership for which a return had been filed to determine whether the three year or the six year statute of limitations applies it

[11] Several changes from existing law have been made in subsection (e) of this section. In paragraph (1), which relates to income tax, the existing 5-year rule in the case of an omission of 25 percent of gross income has been extended to 6 years. The term gross income as used in this paragraph has been redefined to mean the total receipts from the sale of goods or services prior to diminution by the cost of such sales or services. A further change from existing law is the provision which states that any amount as to which adequate information is given on the return will not be taken into account in determining whether there has been an omission of 25 percent. H. Rept. No. 1337, 83d Cong., 2d Sess., p. A-414 (1954).

normally operates to his benefit. *Genevieve B. Walker, supra;* Cf. *Jack Rose, supra;* and *Elliott J. Roschuni, supra.*

Section 6013(e) was adopted in consequence of a series of decisions imposing fraud penalties and taxes upon the spouses of guilty taxpayers, where admittedly the spouse had no knowledge of the fraud and did not benefit economically from it, because joint returns were filed. *Louise M. Scudder,* 48 T.C. 36 (1967) reversed and remanded 405 F. 2d 222 (C.A. 6, 1968); *Huelsman* v. *Commissioner,* 416 F. 2d 477 (C.A. 6, 1969), remanded for disposition within guidelines of Circuit Court opinion; *Betty Bell Wissing (Formerly Betty Bell Huelsman),* 54 T.C. 1428 (1970).[12] See also *Kathleen C. Vannaman,* 54 T.C. 1011 (1970).

In adopting section 6013(e) Congress only provided relief for an innocent spouse where a joint return was filed and all of the other requirements of section 6013(e) were met, including an omission from gross income exceeding 25 percent of the total gross income stated in the return. It did not provide relief for innocent spouses in community property states where no joint returns were filed, even though all the other requirements of section 6013(e) were met. *United States* v. *Mitchell,* 403 U.S. 190 (1971); *Mary Lou Galliher,* 62 T.C. No. 81 (September 3, 1974). In *Mitchell* the Court suggested the remedy was legislation such as sections 6013(e) and 6653(b). Furthermore, Congress did not provide relief if the liability was attributable to improper deductions.[13] Petitioners' liability, in part, was attributable to improper deductions on the partnerships' re-

[12] For a discussion of the background of section 6013(e) see Meade Emory, "New Law Alleviates Innocent Spouse-Joint Return Problem on Omitted Income," 34 Journal of Taxation 154 (1971).

[13] Ibid., Footnote 12.

turns. If Congress could constitutionally exclude from relief innocent spouses in community property states where no joint return was filed, it could properly exclude other innocent spouses who could not meet the tests of section 6013(e)(1)(A).

We think it is constitutionally permissible for Congress to take one step at a time in adopting a relief provision, addressing itself first to the phase of the problem which seems to it most egregious. *Williamson* v. *Lee Optical Co.,* 348 U.S. 483 (1955); *McDonald* v. *Board of Election,* 394 U.S. 802, 809 (1969); *National Labor Relations Board* v. *Jones & Laughlin Steel Corp.,* 301 U.S. 1, 46 (1937). Congress has apparently decided the potential injustice was greatest where an omission from gross income occurred and joint returns were filed. In so limiting its remedy Congress dealt with an appropriate class and it was not bound to include others. *Graham & Foster* v. *Goodcell,* 282 U.S. 409, 431-432 (1931). Cf. *W. Astor Kirk,* 51 T.C. 66 (1968), affd. 425 F. 2d 492 (C.A. D.C., 1970).

We hold petitioners have failed to sustain their burden of overcoming the presumption of the validity of section 6013(e). We also hold that section 6013(e) is constitutional. Having decided the issues before us in favor of the respondent, these cases will be set for trial in due course on the other issues presented by the pleadings.

An appropriate order will be entered.

Statutes Involved

Sec. 6013. Joint returns of income tax by husband and wife.

• • • • •

(e) Spouse relieved of liability in certain cases.

(1) In general.—Under regulations prescribed by the Secretary or his delegate, if—

(A) a joint return has been made under this section for a taxable year and on such return there was omitted from gross income an amount properly includable therein which is attributable to one spouse and which is in excess of 25 percent of the amount of gross income stated in the return.

(B) the other spouse establishes that in signing the return he or she did not know of, and had no reason to know of, such omission, and

(C) taking into account whether or not the other spouse significantly benefited directly or indirectly from the items omitted from gross income and taking into account all other facts and circumstances, it is inequitable to hold the other spouse liable for the deficiency in tax for such taxable year attributable to such omission.

then the other spouse shall be relieved of liability for tax (including interest, penalties, and other amounts) for such taxable year to the extent that such liability is attributable to such omission from gross income.

(2) Special rules.—For purposes of paragraph (1)—

(A) the determination of the spouse to whom items of gross income (other than gross income from property) are attributable shall be made without regard to community property laws, and

(B) the amount omitted from gross income shall be determined in the manner provided by section 6501(e)(1)(A).

Sec. 6501. Limitations on assessment and collection.

• • • • •

(e) Substantial omission of items.

Except as otherwise provided in subsection (c)—

(1) Income taxes. In the case of any tax imposed by subtitle A—

(A) General rule. If the taxpayer omits from gross income an amount properly includible therein which is in excess of 25 percent of the amount of gross income stated in the return, the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time within 6 years after the return was filed. For purposes of this subparagraph—

(i) In the case of a trade or business, the term "gross income" means the total of the amounts received or accrued from the sale of goods or services (if such amounts are required to be shown on the return) prior to diminution by the cost of such sales or services; and

(ii) In determining the amount omitted from gross income, there shall not be taken into account any amount which is omitted from gross income stated in the return if such amount is disclosed in the return, or in a statement attached to the return, in a manner adequate to apprise the Secretary or his delegate of the nature and amount of such item.

Stipulation of Facts

UNITED STATES TAX COURT

Docket Nos. 2696-64
2202-66

ESTATE OF HERMAN KLEIN, Deceased, BEBE KLEIN, MALCOLM B. KLEIN and IRA K. KLEIN, Executors and BEBE KLEIN, Individually,

Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

STIPULATION OF FACTS

The parties hereby stipulate and agree that for the purpose of this case, the following facts and exhibits attached hereto and made a part hereof may be taken as true, subject to the rights of the parties to introduce other and further evidence not inconsistent with this stipulation and preserving the parties' rights to object, at the time of trial, to any and all portions of said stipulation and attached exhibits as they may deem to be irrelevant or immaterial.

1. The petitioners are the Estate of Herman Klein, Deceased, Bebe Klein, Malcolm B. Klein and Ira K. Klein, Executors, and Bebe Klein, as surviving wife. The addresses of the above-named individuals at the time of the filing of the petition were as follows:

(a) Bebe Klein
201 East 83 Street
New York, N.Y.

(b) Malcolm B. Klein
31 Dorchester Street
Huntington Station, N.Y.

(c) Ira K. Klein
107 Jackson Place
Paramus, New Jersey

2. Herman Klein died on August 30, 1964.

3. The Surrogate's Court of New York County on October 19, 1964, granted letters testamentary on the Estate of Herman Klein to Bebe Klein, Malcolm B. Klein and Ira K. Klein, who duly qualified and are presently acting as Executors.

4. Herman Klein and Bebe Klein timely filed a joint return for the taxable year 1955 with the District Director, of the then Upper Manhattan District, New York. Attached hereto and marked Exhibit 1-A is a copy of the petitioners' joint Federal income tax return for the taxable year 1955.

5. Herman Klein, during the year 1955, was engaged in the manufacture of dresses as a 30% partner in the partnerships of Miss Smart Frocks and C & S Dress Company, and as a stockholder in Miss Smart Frocks, Inc.

6. A partnership return, form 1065, for the taxable year beginning May 1, 1954 and ending April 29, 1955 of Miss Smart Frocks and C & S Dress Co., using the accrual method of accounting, was filed with the District Director,

of the then Upper Manhattan District, New York, New York. Attached hereto and marked Exhibit 2-B is a copy of Federal partnership return of Miss Smart Frocks and C & S Dress Co. for the taxable year ended April 29, 1955.

7. The following items were omitted from gross income on said joint return filed by Herman and Bebe Klein:

Dividend income	$21,994.29
Other income	5,200.00
Partnership income	18,495.74
Interest income	43.25
Total amount omitted from Gross income	$45,733.28

8. The said joint tax return filed for the year 1955, shows the following items of gross income:

Interest	$ 191.21
Royalties	494.05
Partnership	90,845.89
Total	$91,531.15

9. For the year 1955 the amount omitted from gross income (paragraph 7 herein) totaling $45,733.28, exceeds 25% of the items of gross income shown in the return (paragraph 8 herein) totaling $91,531.15.

10. The parties agree that Bebe Klein meets the requirements of the *Int. Rev. Code of 1954*, § 6013(e)(1)(B) and (C).

11. For the year ending April 29, 1955, the partnership return of Miss Smart Frocks and C & S Dress Co., showed sales of $3,545,911.95; a schedule contained therein of C & S Dress Company for the same year showed gross income from contracting of $141,457.40.

12. The petitioners' 1955 joint tax return did not show therein the items described in paragraph 11.

13. For the year 1955, the amount omitted from gross income (paragraph 7 herein) totaling $45,733.28) does not exceed 25% of the sum of $1,106,896.07 which is composed of the following items:

Interest	$ 191.21
Royalties	494.05
Partnership (30% distributive share of the sales and contracting income of Miss Smart Frocks and C & S Dress Company	$1,106,210.81
Total	$1,106,896.07

14. The parties agree that Bebe Klein is not liable for any addition to tax under the provisions of *Int. Rev. Code of 1954*, § 6653(b) for the taxable year 1955.

PAUL M. LEVINSON
Counsel for Petitioners.

(Sgd) MEADE WHITAKER—CCMJr.
MEADE WHITAKER,
Chief Counsel,
Internal Revenue Service.